

# **Before You Sign on the Dotted Line. . .**

## **Questions for Farmers to Ask Before Entering Into a Direct Marketing Agreement**

PAGE 1

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Many farmers who have shifted to direct marketing their products pride themselves on their personal relationships with their buyers. These personal relationships are a real strength of the direct marketing movement. At the same time, as farmers increase the scope and sophistication of their direct marketing efforts, they may find that agreeing on a price and quantity with the buyer and shaking hands on the deal does not do enough to anticipate all of the questions that may arise later. The buyer may offer a written contract to the farmer, or the farmer may want to offer a written contract to the buyer.

These materials help identify the questions that commonly arise when farmers enter into partnerships with buyers—whether they be wholesalers, cooperatives, restaurants, grocery stores and food co-ops, florists, or other farmers. Many farmers state that having a written contract gives them a greater sense of stability, and enables them to produce a business plan with greater confidence of its accuracy.

### **What “counts” as a contract?**

Many producers have questions about whether an oral agreement “counts” as a contract. Parties are always free to carry out otherwise lawful oral agreements.

Questions arise when one party wishes to force the other party to fulfill its promises.

Some agreements must be in writing to be enforceable. In general, agreements that cannot be completed within one year must be in writing to be enforceable. A contract for the sale of goods of over \$500 may need to be in writing in order to be enforceable. If the contract is subject to a rule requiring it be in writing in order to be enforced, there must be a written contract in order for a court to resolve any problems that arise.

A written contract need not discuss all of the items discussed below. In general, a written contract should identify the parties to the contract, identify the subject matter and terms and conditions of the contract, including the price and quantity of goods to be exchanged.

### **Does having a written contract mean the buyer and seller don't trust one another?**

Some farmers who market their products fear that asking for written agreements will be received as an expression of mistrust. However, the main problem with oral agreements is not unfair or sharp business practices, but simple confusion and misunderstandings.

Most disputes about contracts are the result of two basically honest parties having different needs and interests, which may lead to different understandings of the meaning of the agreement itself. These difficulties are compounded if the parties are forced to rely upon their memories of an oral agreement. Few people's memories are good enough to recall all of the

important details of an agreement.

What is more, even the most honest and trusting relationships can change through no fault of the farmers or their buyers. Restaurants change hands or hire new chefs, distribution centers are closed. The list of possible problems is long. Keeping good records of dealings with buyers is a little like buying insurance. It is done not because farmers expect to have problems, or because they are eager to go to court, but because in the rare instance in which farmers do have serious problems with buyers, it will be extremely important to be able to prove exactly what the parties agreed to do.

### **What are some other recordkeeping suggestions?**

It is a good idea to keep copies of all documents (such as invoices, packing lists, delivery logs, and payments) and note the date they were signed, sent, or received. Many buyers pay for agricultural products only after they have received an invoice. It is important for farmers to send invoices promptly. Some producers make a habit of writing a letter describing every important conversation with the buyer and keeping a copy for themselves. These letters may ask the buyer to respond in writing by a certain date if the buyer disagrees with anything the producer has said about the conversation. In order to verify that the letters were sent and received, some producers mail them by certified mail, return receipt requested, and keep evidence of the receipt.

### **What should farmers look for in a contract proposed by the buyer?**

The best time for a producer to weigh the pros and cons of the contract being negotiated is before the producer borrows large sums of money, mortgages his or her farm and home, or foregoes other opportunities. Having a written contract to review emphasizes to the producer that an important decision-making stage has been reached.

The first step in reviewing a contract is to read it carefully. Farmers should make sure that they know how the contract addresses the important issues that may arise. If there is any doubt about the meaning of contract terms, farmers should consult an attorney licensed to practice law in their state. After a contract is signed, a farmer should keep it with other important records. This way it can readily be referred to should any questions arise. Some farmers make a habit of re-reading their contracts regularly, even in the absence of any dispute.

### **What if a farmer doesn't want to agree to some of the terms in the contract the buyer offers?**

Many large buyers use pre-printed form contracts in their purchasing of agricultural products. Farmers may not wish to agree to some provisions in the form contract. It is perfectly acceptable for the farmer to ask the buyer whether those provisions can be taken out of the contract. The farmer's negotiating power is usually greatest before signing the contract. If the buyer agrees to the farmer's request, the provisions may be crossed out of both the buyer's and seller's copies of the contract. It is a good practice for each party to initial the place where the provision was crossed out on both copies. In the alternative, a new contract may be prepared. If the buyer does not agree to the changes requested by the farmer, the farmer must either accept or reject the contract as offered by the buyer.

### **Can farmers write their own contracts to offer to the buyer?**

Yes. A contract need not be written by a lawyer in order to be valid. Simple language is often adequate. However, the contract should include all of the terms agreed to by the parties, and should include sufficiently detailed information to describe the parties' agreement. Farmers may want to consult an attorney if it is their first time offering a written agreement, if the deal is particularly complicated, or if the deal is for a particularly large portion of the farming operation's income.

### **What does it mean to have an enforceable contract?**

An enforceable contract is one that meets all of the requirements of applicable state law and that would be recognized as binding in state court. In general, a person who wishes to enforce a contract must file an action in state court. If the court finds that buyers or sellers have not done what they agreed to do in the contract, the court will generally award the other party a remedy. Remedies for breach of contract vary. A court may order "specific performance," in which a party that breached a contract is ordered to do what it said it would do. Or a court may order a party it finds has breached a contract to pay the other party money damages. In many cases, the court will ask whether the other party took steps to "mitigate the damage." For example, if a farmer had a one-year contract for the sale of eggs, and the buyer breached the contract by stating it would not accept the eggs for the last six months of the contract, the court may ask for evidence that the farmer tried to find other buyers in order to reduce the harm suffered.

Many farmers state that they would never sue their buyers. Most farmers would rather reach resolution of disputes outside of the courtroom, such as through negotiation or mediation. The costs of litigation—in terms of out-of-pocket costs and attorney fees, time, and damaged relationships—may be greater or less than the amounts that could be recovered. These are important considerations to take into account, and may counsel against taking a breach of contract dispute to court. Yet having a contract that *could* be enforced in court gives farmers more options and can actually assist farmers in resolving disputes without resorting to the court system. If the amount in dispute is relatively small, many states have small claims courts.

The greatest advantage of reducing an agreement between buyer and seller to writing is probably not the ability to file a lawsuit, but in the disputes the practice prevents. Discussing a deal in detail helps both parties to identify misunderstandings and either resolve them or decide not to make the deal.

### **Questions to Discuss with Your Buyers**

Listed below are some terms and conditions commonly addressed in contracts for the sale of agricultural products.

**Title and Purpose.** A title can provide important information about the contract. For example, "Agreement for the Sale of 2005 Soybean Contract." Contracts often include a brief statement of the purpose of the contract as well.

**Definitions.** Many contracts define certain terms used in the contract. These are

helpful if a term could be interpreted in more than one way. For example, does “cattle” refer only to Black Angus, or might Red Angus, Herefords, or Charlois be acceptable? If the contract is for the sale of “large” watermelons, what does that mean? If a “large” watermelon weighs 22 pounds, must every watermelon be exactly that size, or should the watermelons be an average of 22 pounds? Will the buyer accept some “small” watermelons? Is there a weight/size the buyer won’t accept?

**Parties.** Most contracts identify the parties in some way. Must the products be supplied by a specific farmer or farming operation, or can an order be fulfilled by any member of a producer group?

**Assignment.** Some contracts state that the buyer may freely assign the contract.

This means that the buyer could be sold or merge with a larger company, and your contract would be transferred to the new owners. May the producer assign the contract, or must the buyer’s permission be obtained first?

**Quantity.** A basic element of a contract for the sale of agricultural goods is quantity. This may be measure in bushels, pounds, acres, etc. A buyer’s statement that, “We’ll take everything you’ve got” can lead to disappointment for either party. What happens if the buyer’s market changes? Or the producer’s yield is unusually high or low?

**Price.** Another basic element of a contract for the sale of agricultural goods is price.

**Prompt payment.** When will the buyer make payment? If the buyer’s terms are 30 days net, when do the 30 days begin? Will the buyer make a partial payment in advance, or pay cash on delivery? If the buyer fails to pay promptly after delivery, will the buyer pay interest? Is the farmer protected by the federal Perishable Agricultural Commodities Act or Packers and Stockyards Act, or by any state laws?

**Length of the contract.** Every contract should state how long it lasts, or how it may be ended.

**Farming Practices.** Are there production deadlines? Do the farmer and buyer agree that certain farming practices must be used? Must the farm be certified organic, or have other third party certification? Does the producer agree to farming practices he or she can control, or does the contract commit the producer to results he or she may not be able to control? Compare a contract in which the producer agrees to plant seed that is certified as free of genetically modified organisms (GMO’s) and to take reasonable steps to prevent GMO drift onto his or her fields, to a contract in which the producer agrees to sell soybeans that are “GMO-free.”

**Quality.** Does the buyer reserve the right to reject inferior products? Who decides if it’s an inferior product? If the buyer rejects the products, what happens to them? Will they be sent back to the producer? Who pays for shipping? Should the buyer try to sell them at a lower price?

**Grading and Weighing.** Does the contract require products of a certain grade, or is payment based upon weight? If so, who will perform the grading or weighing? May others observe? Are there specifications for the type of scale to be used? Who will pay any costs for the grading or weighing?

**Packaging.** How should the agricultural products be packaged? For example, if blueberries must be packaged in pint-sized clamshell containers, the producer’s costs for labor and supplies may result in a different price than if the blueberries are sold by the bushel.

**Processing.** How should the agricultural products be processed? This is of particular concern for livestock producers, and is a key factor in pricing. Is the price for live weight? Hanging weight? Is it per pound of tenderloin or per pound of round roast?

**Delivery terms and schedule.** Who is responsible for delivering and unloading the products? Will the buyer have someone present to provide access to suitable storage facilities?

**Shipping costs.** Who pays for these? Are there special rules for rush orders?

**Losses in transit.** Who pays for these?

**Natural Disaster losses.** If the producer's crop is damaged or destroyed as a result of a natural disaster, what happens? Must the producer make a payment to the buyer? Must the producer go and buy the products elsewhere? May the producer do so? Must the buyer go and try to buy the products elsewhere? May the buyer bill the producer for any higher costs associated with obtaining the substitute products? If applicable, the contract may also address losses associated with mechanical failures.

**Entirety clause.** In general, if two parties enter into a written contract, it is assumed that all of the agreements reached by the parties are included in the contract. Some contracts include an "entirety clause," which formally states that the written contract is the entire agreement between the parties. This means that oral statements related to the subject of the contract made by either party are generally not enforceable.

**Ending the contract.** The contract may specify a date at which the contract ends. It may also state other ways it can be terminated and what notice is required before termination. Does each party have a way to terminate the contract? Some contracts provide that they may be terminated for any reason. Other contracts say that they may only be terminated for good cause.

**Renewing or renegotiating the contract.** The contract may state how it can be renewed or modified. Changes to the contract should be made in writing and signed by both parties. Perhaps the price of seed or other supplies will change, or perhaps demand will increase or decrease.

**Alternative Dispute Resolution (ADR).** Some contracts set out how any disagreements between the producer and the buyer must be handled. The contract may call for the use of Alternative Dispute Resolution, such as mediation or arbitration. Mediation is an attractive option to some, because it employs a neutral third party to help the parties to discuss the disputed issue. This can help the parties resolve problems while preserving the relationship. Mediation is not binding, so if one or more of the parties are not satisfied, they may still take the dispute to court.

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## What are some other sources of information?

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- Iowa Attorney General, Grain Production Contract Checklist, Livestock Production Checklist, and Contracts. These are short and helpful lists of things that might be included in a contract. The web site also includes many marketing, production, and purchasing contracts. [http://www.state.ia.us/government/ag/working\\_for\\_farmers/contracts.html](http://www.state.ia.us/government/ag/working_for_farmers/contracts.html).
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